

UNITED STATES OF AMERICA
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Competitive Product Prices
Inbound Competitive Multi-Service Agreements
with Foreign Postal Operators 1 (MC2010-34)
China Post Group

Docket No. CP2014-39

PUBLIC REPRESENTATIVE COMMENTS ON POSTAL SERVICE
NOTICE CONCERNING ADDITIONAL INBOUND COMPETITIVE
MULTI-SERVICE AGREEMENTS WITH FOREIGN POSTAL
OPERATORS 1 NEGOTIATED SERVICE AGREEMENT

(April 17, 2014)

The Public Representative hereby provides comments pursuant to Order No. 2405.¹ In that Order, the Commission established the above referenced docket to receive comments from interested persons, including the undersigned Public Representative, on a Postal Service Notice of its entering into an additional Inbound Competitive Multi-Product Bilateral Agreement with China Post Group.² (China Post 2014 Agreement) that the Postal Service seeks to include within the Inbound Competitive Multi-Service Agreement with Foreign Postal Operators (MC2014-34) product. On December 21, 2012, the Commission approved the addition of the China Post 2013 Agreement to the Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 product.³ The Commission subsequently approved an amendment to the contract in Docket No. CP2013-23.⁴

The China Post 2014 Agreement includes rates for the delivery of inbound Air Parcel Post (Air CP), Surface Air Lifted Parcels, Surface CP, Express Mail Service

¹ PRC Order No. 2405, Notice and Order Concerning Additional Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 Negotiated Service Agreement, April 11, 2014.

² Notice of United States Postal Service of Filing Functionally Equivalent Inbound Competitive Multi-Service Agreement with a Foreign Postal Operator, November 30, 2012, (Initial Notice) at 1.

³ PRC Order No. 1591, Order Approving an Additional Inbound Competitive Multi-Service Agreements with Foreign Operators 1 Negotiated Service Agreement (with China Post Group), December 21, 2012.

⁴ PRC Order No. 1752, June 18, 2014.

(EMS) by the Postal Service and a yet-to-be launched inbound product. Initial Notice at 4. In this proceeding, the Postal Service's Notice provides a redacted copy of the signed agreement, a copy of the Governors' decision authorizing the product, a certification of compliance with 39 U.S.C. 3633(a) an application for non-public treatment of certain materials. It also filed supporting financial workpapers. The China Post Agreement is intended to become effective on May 1, 2014 and to remain in effect until June 30, 2015 unless terminated sooner.⁵

COMMENTS

The Public Representative has reviewed China Post 2014 Agreement and the supporting financial model filed under seal that accompanies the Postal Service's Notice. Based upon that review, the Public Representative concludes that the China Post 2014 Agreement appears likely to satisfy the requirements of 39 U.S.C. § 3633. That said, the projected cost coverage presented in the financial model for the Agreement is small and there is little margin for error if unit costs, especially for inbound EMS, are understated. However, the inclusion of cost contingency factors does provide an additional element of security that a sufficient level of cost coverage will be attained.

Requirements of 39 U.S.C. § 3633. Pursuant to 39 U.S.C. § 3633(a), the Postal Service must demonstrate that the China Post 2014 Agreement covers its attributable costs, and thereby precludes the subsidization of competitive products by market dominant products. As indicated above, the Postal Service's financial model for the Agreement indicates that the negotiated prices, including those for the new air parcel products, will generate sufficient revenue to cover costs.⁶ However, the estimated mail processing and delivery unit costs shown in the financial model for both new air parcel products do not appear reasonable.

⁵ Initial Notice at 4.

⁶ It should be noted that the projected cost coverage shown in the financial model for the instant Agreement is an improvement over the projected cost coverage for the China Post 2013 Amended Agreement shown in the financial model accompanying the Postal Service's Initial Notice. *Compare* Excel files China_Comp_IB_2013.05.23.xls, worksheet tab 15_Proj_Cost & Revenue, and China_Comp_IB_2014FINAL.xls, worksheet tab 15_Proj_Cost & Revenue.

The Postal Service separately estimates the mail processing and delivery unit costs of the Signature Confirmation and Delivery Confirmation services.⁷ To estimate the mail processing and delivery unit costs for the new air parcel products with Signature Confirmation and Delivery Confirmation, the financial model adjusts the average mail processing and delivery unit costs for inbound air parcel post from all developing countries presented in the FY2013 International Costs and Revenue Analysis (ICRA) report.⁸ For the new air parcel product with Signature Confirmation, however, no adjustments are made as the financial model assumes that the mail processing and delivery unit costs for this new product are the same as the average unit costs for inbound air parcel post from all developing countries. For the new air parcel product with Delivery Confirmation, the financial model adjusts the average unit costs downward by the estimated mail processing and delivery unit costs of the Delivery Confirmation service, thereby making the mail processing and delivery unit costs for this new product even less than the average unit costs for inbound air parcel post from all developing countries.

The mail processing and delivery unit cost estimates for the new air parcel products with Signature Confirmation and Delivery Confirmation are counter intuitive, *i.e.*, the mail processing and delivery costs are less expensive for the air parcel products with additional services than those products would be without such services. The Commission should request from the Postal Service an explanation for these counter intuitive estimates.

Even apart from issues with the costing methodologies for the new air parcel products is the issue of whether it is even proper to include these products in the cost coverage calculations in the first place. This issue was addressed by the Public

⁷ See Excel file China_Comp_IB_2014FINAL.xls, worksheet tab 01_Inputs. It should be noted that the financial model does not show how the separately estimated mail processing and delivery unit costs of Signature Confirmation and Delivery Confirmation are developed. Rather, these unit cost estimates are taken from two Excel spreadsheets, SIGCon-FY 2012.xls and DelCon-FY 2012.xls, which were not provided to the Commission with the financial model. The Commission should request that the Postal Service provide these Excel files in order to obtain the entire financial model relied upon by the Postal Service in developing its unit cost estimates for the new air parcel products.

⁸ Excel file China_Comp_IB_2014FINAL.xls, worksheet tab 05_Product_Unit_Cost_Inputs, Note "Source: [Ab] to [Cb] and [Ae] to [Ce]," *citing* (USPS-FY13-NP2, Docket No. ACR2013, Revised 2/6/2014), Reports.xls file, 'CRA Staging' tab (Developing Country Costs).

Representative in the prior China Post Agreement. In that Docket, the Public Representative expressed her concerns with the inclusion of this ‘yet-to-be launched inbound product’⁹ for which very little information is provided, as part of the calculations of the Agreement’s overall cost coverage. *Id.* The Public Representative concurs with this opinion. In addition, in Docket No. CP2013-23, the Public Representative noted that correcting the various methodological flaws she detected, could worsen the projected cost coverage under the contract. *Id.* In the instant docket, it appears that not including the yet-to-be launched inbound products in calculating the projected cost coverage under the contract, could actually *increase* the projected cost coverage under the contract. If it could be known with any degree of certainty that these products would be launched during the pendency of the contract, it would be appropriate to include them in the projected cost coverage calculations. However, since they still remain, even in the successor contract which is the subject of this docket, as ‘yet-to-be launched’, it would seem to be quite speculative to include them in the projected cost coverage calculations.

Functional Equivalence. The Postal Service asserts that the inbound portion of the China Post 2014 Agreement is substantially similar to the inbound portion of the China Post 2013 Agreement, which was an agreement between the same two parties that had similar cost characteristics and concerned similar types of products. It is also asserts that like the China Post 2013 Agreement, the China Post 2014 Agreement also fits within the parameters outlined by Governors Decision No. 10-3, which establishes the rates for Inbound Competitive Multi-Service Agreements with Foreign Postal Operators. There are differences between the inbound portion of the China Post 2014 Agreement and the inbound portion of the China Post 2013 Agreement. The Postal Service does not consider that the specified differences affect either the fundamental service the Postal Service is offering or the fundamental structure of the agreements. The Public Representative agrees with the Postal Service’s assertion of Functional Equivalence of the China Post 2014 Agreement with the China Post 2013 Agreement.

⁹ Public Representative Comments in Docket No. CP2013-23, December 12, 2012, at 4.

The Public Representative respectfully submits the foregoing comments for the Commission's consideration.

Kenneth R. Moeller
Public Representative

901 New York Ave. NW
Washington, DC 20268-0001
202-789-6888
Kenneth.moeller@prc.gov